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No. 296

In the Supreme Court of the United States

OCTOBER TERM, 1961

CHRYSLER CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	1
Statutes involved	2
Statement	3
Argument	6
Conclusion	8

CITATIONS

Case:	
Security Mills Co. v. *Commissioner*, 321 U.S. 281	7
Statutes:	
Internal Revenue Code of 1939:	
Sec. 41 (26 U.S.C. 1952 ed., Sec. 41)	2, 7
Sec. 43 (26 U.S.C. 1952 ed., Sec. 43)	2, 7
Miscellaneous:	
Divergences Between Rules of Tax Accounting and Generally Accepted Accounting Principles, 97 Journal of Accountancy 93 (1954)	7–8

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OPINIONS BELOW

The opinion of the Tax Court (Pet. B1–B29) is reported at 33 T.C. 843. The opinion of the Court of Appeals (Pet. A1–A2) is reported at 289 F. 2d 643.

JURISDICTION

The judgment of the Court of Appeals was entered on May 11, 1961. The petition for a writ of certiorari was filed on August 9, 1961. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED

May a taxpayer corporation deduct in the year of an employee's retirement not merely the annual pre-

mium upon, but the full face value of, a life insurance policy which it is required by contract to furnish at its own expense?

STATUTES INVOLVED

Internal Revenue Code of 1939:

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in section 48 or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year.

(26 U.S.C. 1952 ed., Sec. 41.)

SEC. 43 [as amended by Sec. 134(b), Revenue Act of 1942, c. 619, 56 Stat. 798]. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits (other than the corporation dividends paid credit provided in section 27) provided for in this chapter shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in

order to clearly reflect the income the deductions or credits should be taken as of a different period. In the case of the death of a taxpayer whose net income is computed upon the basis of the accrual method of accounting, amounts (except amounts includible in computing a partner's net income under section 182) accrued as deductions and credits only by reason of the death of the taxpayer shall not be allowed in computing net income for the period in which falls the date of the taxpayer's death.

(26 U.S.C. 1952 ed., Sec. 43.)

STATEMENT

Taxpayer, a Delaware corporation, keeps its books and files its returns on a calendar year basis, using an accrual method of accounting (Pet. B1).

Prior to 1950, taxpayer held a one-year renewable group life insurance policy with Aetna Life Insurance Company for the benefit of all of taxpayer's active employees who contributed to the cost of the insurance. At that time, taxpayer was not obligated to provide life insurance coverage for its retired employees, and it did not do so (Pet. B1–B2).

During 1950, the taxpayer entered into a collective bargaining agreement with various unions. The basic agreement required the taxpayer to endeavor in good faith to acquire life insurance coverage at company expense for certain qualified employees upon their retirement (Pet. B2–B6). Pursuant to that agreement, taxpayer acquired from Aetna a one-year renewable term, nonparticipating insurance policy to take effect August 1, 1950 (Pet. B6–B7). Under its terms, qualified retiring employees would receive life insurance

in the face amount of $1,000, $750, or $500, respectively, depending upon the number of years of the employee's service. Retired employees were not required to contribute towards the cost of that insurance, but active employees were to make contributions (Pet. B8–B9). Upon an employee's retirement, Aetna would issue to him a certificate stating the amount of life insurance to which he remained entitled as long as the policy was in effect (Pet. B13).

At all times since the policy went into effect, taxpayer has made payment to Aetna in accordance with the latter's experience rating plan. Under that plan, Aetna would estimate at the beginning of each policy year the amount of premiums necessary for that year, which amount was paid by taxpayer in monthly installments. At the end of the policy year, Aetna determined the actual necessary premiums for the year. This figure represented the sum of (1) the amount of claims incurred by Aetna as a result of the death of active and retired employees covered by the policy, (2) the cost to Aetna of the conversion privileges exercised by taxpayer's employees, and (3) Aetna's charge for services rendered. If the amount of the necessary premium was smaller than the amount paid by taxpayer during the year, the difference was either refunded to taxpayer or credited to it as payment of other insurance coverage. However, if there was a deficit, it was either charged to an account maintained by taxpayer or carried forward and charged against some future year (Pet. B14).

By December 31, 1951, there were 672 retired employees of taxpayer, still living, who were covered by

the policy. The total face amount of life insurance for those employees was $566,750. Of those employees, 290 had retired during the period August 1 through December 31, 1950, and the total amount of their coverage was $255,000. The remaining employees (382) retired during 1951, with a total life insurance coverage of $311,750 (Pet. B15).

During December 1951, taxpayer debited to expense $566,750, *i.e.*, the total face amount of insurance coverage under the policy for retired employees who were still living at that date, and deducted that amount from its federal tax return for 1951. The Commissioner disallowed that deduction and determined that taxpayer could properly deduct only the amount of premiums accrued during the taxable year (Pet. B15–B16). Accordingly, the Commissioner determined a deficiency for that year in the amount of $457,650.62 (Pet. B1). Taxpayer then brought this action in the Tax Court seeking a redetermination.

In the Tax Court, taxpayer conceded that $255,000 of the amount it had sought to deduct was attributable to the 290 employees who had retired *prior* to 1951 and, therefore, could not be accrued in that year. Accordingly, taxpayer has limited its claim for a deduction to the balance, *i.e.*, $311,750, and only that amount is in dispute here [1] (Pet. B18).

The Tax Court held for the Commissioner and the Sixth Circuit affirmed (Pet. A1–A2, B1–B29).

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[1] In the Tax Court, taxpayer also contended unsuccessfully that it had overpaid its taxes for the year 1951 in the additional amount of $719,091.67. However, taxpayer expressly abandoned that contention on appeal and, consequently, that item is no longer in dispute.

ARGUMENT

Taxpayer seeks to accrue, as an expense on the date an employee retires, an amount equal to the face value of the retired employee's life insurance. It attempts to justify that treatment on the theory that, under the payment plan of the Aetna policy held during the taxable year (1951), it is in effect a self-insurer in that the total amount it will pay as premiums on the insurance policies of all of its retiring employees will average out to approximately the total face value of the insurance policies.

There is, first of all, no adequate support for taxpayer's premise. The Tax Court found (Pet. B23–B26) that, because of the contributions to premiums made by the active employees, it was by no means certain that taxpayer would incur this expense *in toto*. Moreover, while the union agreement obligates taxpayer to provide life insurance for its retired employees, it was not obligated to hold the Aetna policy or to use the premium payment plan which was in effect during the taxable year. As the policy was for a one-year renewable term, taxpayer could choose a new policy with a different payment plan at some future date and thereby relieve itself of the burden that it carried as a self-insurer. It therefore had no fixed liability, as of the taxable year, in an amount equal to the face value of the retiring employees' insurance.

Taxpayer could not deduct the total face amount of the retiring employees' insurance in the year of retirement even assuming that in that year there arose a fixed obligation on taxpayer's part to pay an amount

equal to the face value of the insurance at some future date. Sections 41 and 43 of the Internal Revenue Code of 1939, *supra*, pp. 2–3, permit an accrual basis taxpayer to deduct its expenses in the year of accrual according to the method of accounting regularly employed by the taxpayer *unless* that method does not clearly reflect income. Taxpayer's accrual of the instant item does not in fact clearly reflect income. An amount equal to the face value of the retiring employee's insurance will be incurred by taxpayer as an expense, if at all, over a period of *many* years, *i.e.*, the period of life remaining to the 382 employees who retired during the taxable year. Thus, taxpayer seeks to lump into one year and take as a deduction anticipated expenses that will be incurred far in the future, if ever. This Court expressly prohibited such accounting treatment for tax purposes in *Security Mills Co.* v. *Commissioner*, 321 U.S. 281, 285, where the Court held that the purpose of the qualifying language in Section 43 was to prevent the deduction in one year of a fixed liability payable in installments over a series of years.[2]

Finally, it appears that taxpayer's method of accounting does not even conform to established commercial accounting principles. In their recommendations to Congress regarding *Divergences Between Rules of Tax Accounting and Generally Accepted Accounting Principles*, 97 Journal of Accountancy 93 (1954), the American Institute of Accountants (AIA) summarized generally accepted accounting principles.

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[2] The Court was there dealing with Section 43 of the Revenue Act of 1934, c. 277, 48 Stat. 680, which is virtually identical to Section 43 of the Internal Revenue Code of 1939, here involved.

As to the issue here involved, the AIA stated (97 Journal of Accountancy, *supra*, p. 95):

> Costs and expenses directly identifiable with revenues are chargeable against the income of the period in which the revenues are recognized. Expenses, such as insurance, rent, property taxes and interest, which are for particular periods of time are chargeable over such periods. Other expenses incurred in the general conduct of the business are chargeable against the income of the period in which they are incurred unless it is clearly evident that they are for the benefit of future periods and there is a reasonable basis, both as to amount and time, for allocating them to future periods, in which event they should be deferred and charged to such periods.

The decision below is therefore plainly correct. The cases cited by petitioner as conflicting involve substantially different factual situations and thus provide no reason for this Court to undertake a third review of the soundness of the taxpayer's accounting methods.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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